IN THE UNITED STATES BANKRUPTCY COURT

FOR THE

SOUTHERN DISTRICT OF GEORGIA
Savannah Division

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| IN RE: | ) | Chapter 7 Case |
| | ) | Number 85-40555 |
| DIAMOND MANUFACTURING COMPANY, INC. | ) | |
| | ) | |
| Debtor | ) | |
| | ) | |
| W. JAN JANKOWSKI, CHAPTER 7 TRUSTEE | ) | FILED |
| | ) | at 11 O'clock & 15 min. P.M. |
| | ) | Date: 2-17-95 |
| Movant | ) | |
| vs. | ) | |
| | ) | |
| SIGNET COMMERCIAL CREDIT CORPORATION, DONALD E. AUSTIN, DIAMOND MANUFACTURING COMPANY, INC., ROSE MARINE, INC. AND GEORGE N. P. PAHNO, | ) | |
| | ) | |
| Respondents | ) | |

**ORDER**

Before me is the "Trustee's Motion for Reconsideration of Order Entered December 6, 1994 and Statement of Extent of Section 552(b) Claim Against Settlement Fund" dated December 14, 1994, filed

in response to order dated December 6, 1994[1]. The Trustee argues in this motion, contrary to my finding in the December 6 order that under the terms of the May 19, 1994 consent order the lien of Signet Commercial Credit Corp. ("Signet") against the lease attached to the Settlement Fund, that in fact the consent order was intended by all parties to preserve the Trustee's ability to contest Signet's lien against the lease or the Settlement Fund itself. As the Trustee has introduced no new evidence to disturb my finding, the motion to reconsider this portion of the December 6 order is ORDERED denied.

The Trustee also requests that I alter or amend my order of December 6 to clarify the prohibition found therein from paying any administrative expenses. No administrative expenses may be paid without express authorization from this court obtained on application for payment of such. Additionally, with all future requests for authorization for payment of administrative expenses, the trustee shall state the need for immediacy, if any, of payment of the expenses so requested. I will evaluate future requests for payment of administrative expenses based in part on the demonstrated need for immediate payment. The request to alter or amend the order

[1]This order approved the requested attorney's fees and expenses as general administrative expenses, denied payment of administrative expenses from the GPA Settlement Fund until resolution of the Trustee's § 506(c) and § 552(b) claims against the Settlement Fund, and required the Trustee to file a statement of the extent of his claim against the Settlement Fund.

of December 6 as to the prohibition against payment of administrative expense is ORDERED denied. Any future requests for payment will be considered in each such application.

The Trustee also requests that the entire Settlement Fund be made available to the estate as an unencumbered asset in partial repayment of the expenses to the estate of litigating and settling the various environmental claims arising out of the shipyard lease[2], under the "equities of the case" exception to 11 U.S.C. § 552(b).[3] This Code section allows a pre-petition security interest to attach to after-acquired property that is proceeds, product, offspring,

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[2]In the December 6 order, I found that the estate had expended $667,451.78 on the leasehold and the environmental claims associated with the leasehold up to the time of the order.

[3]11 U.S.C. §552(b) provides

> (b) Except as provided in section 363, 506(c),, 522, 544, 545, 547, and 548 of this title, if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, product, offspring, rents, or profits of such property, then such security interest extends to such proceeds, product, offspring, rents, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable nonbankruptcy law, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise.

rents or product of pre-petition collateral if the security agreement provides for such attachment "except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise." I referred to the possibility of recovery under § 552(b) in the December 6 order first raised by the Trustee in brief submitted in support of his original application, but found that the notice and hearing requirement had not been met. The order required that any party in interest desiring to offer further evidence or argument regarding any claim of the Trustee to recover under § 552(b) be filed. No party requested further hearing. The notice and hearing requirement for recovery under the "equities of the case" exception to § 552(b) has been satisfied. The Trustee argues that under the "equity exception" the Settlement Fund should not be subject to the lien of Signet but rather should be made available to the estate. I agree with the Trustee that the equities of this particular case require this result.

While the United States Court of Appeals for the Eleventh Circuit has not yet decided a case controlling an analysis of the exception found in § 552(b), Chief United States Bankruptcy Judge Lamar W. Davis, Jr. of this district has and determined that

> [t]he situation where the value of the collateral increases due to debtor's expenditures and efforts is just one example where the court may apply the "equity exception" and is not the only situation where

> Section 552(b) may be applied. [Cit. omitted] Clearly a bankruptcy court has discretion "to find an appropriate balance between the rights of secured parties and the rehabilitative purposes of the Code. [Cit. omitted]

In re Topgallant Group, Inc., Ch. 7 Case No. 89-41997 slip op. at 11 (Bankr. S.D. Ga. Davis, C.J. Dec. 23, 1992). Additionally,

> [u]nder the equity exception in section 552(b), the secured party should not receive a windfall benefit when the trustee uses assets of the estate, for example, to finish uncompleted inventory (which is proceeds of collateral acquired by the debtor prepetition) subject to a prepetition security interest. In such a case, the trustee may recover from the inventory or its proceeds whatever amounts, after notice and a hearing, the court deems equitable under the circumstances of the case.

4 Collier on Bankruptcy, ¶ 552.02 at 552-11-12 (15th Ed. 1994). See also In re Cross Baking Co., Inc., 818 F.2d 1027, 1033 (1st Cir. 1987) (concluding that the "equities of the case" exception is legislative attempt to address instances where expenditures of the estate enhance the value of proceeds which, if not adjusted, would lead to an unjust improvement of the secured party's position); accord, J. Catton Farms v. First National Bank of Chicago, 779 F.2d 1242, 1246 (7th Cir. 1985); In re Airport Inn Associates, Ltd., 132 B.R. 951, 959 (Bankr. D.Colo. 1990); In re Anderson, 137 B.R. 819, 821-2 (Bankr. D.Colo. 1992). Applying this persuasive authority I

find that the "equity exception" establishes in this case that to avoid an unjust benefit to the secured party, Signet, at the expense of the estate, the Settlement Fund should not be subject to Signet's lien but rather should remain an asset of the estate, as partial reimbursement of expenses incurred in negotiating and executing the Settlement Agreement, unencumbered by Signet's lien.

The first equitable consideration is the clear benefit to Signet of the Settlement Agreement. The Settlement Agreement provided for termination of the lease and assumption by the lessor of responsibility for all environmental contamination. Prior to execution of the Settlement Agreement, Signet held a security interest in the lease.[4] The settlement freed Signet of any potential liability for the cleanup. See, United States v. Fleet Factors Corp., 901 F.2d 1550 (11th Cir. 1990). Additionally, it would be inequitable to supplement this clear benefit to Signet with the added benefit of a continued security interest in the Settlement Fund, an unjustifiable improvement in Signet's position as a secured creditor. Once the Settlement Agreement was executed, the valueless

[4]In the December 6 order, I found that the lease, while initially estimated to have a value of approximately $2.5 million, actually represented a liability to the estate. The trustee, and subsequently this court, first learned of this liability when a contract to sell the lease was being negotiated, in connection with which the first environmental assessment was conducted on the property. The assessment revealed the contamination and follow up study estimated cleanup ranged (as I noted in the December 6 order) from $2.3 to $10 million.

leasehold was replaced by the $300,000 Settlement Fund. The obvious inequity of this result is made clear considering that such an improvement in Signet's position was made possible only after a $667,451.78 expenditure by the estate. Equity demands that the Settlement Fund be used to partially reimburse the estate for expenses incurred in connection with the leasehold and Settlement Agreement. The Settlement Agreement leaves Signet in an improved position by freeing it of all potential cleanup liability without cost (prior to the settlement the lease was without value) and partially alleviates the financial burden sustained by the estate in settling this costly environmental problem. This is the most equitable result that is available under the circumstances.

IT IS THEREFORE FURTHER ORDERED that the lien of Signet on the Settlement Fund is STRICKEN; and

further ORDERED that the Settlement Fund of $300,000.00 plus all accrued interest is a general, unencumbered asset of the estate.

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JOHN S. DALIS
UNITED STATES BANKRUPTCY JUDGE

Dated at Augusta, Georgia
this 17th day of February, 1995.